BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
CREDIT BUREAU CENTRAL, INC.)

For Appellant: R. E. Brown
Chairman of the Board
Southern Daisy Industries, Inc.

For Respondent: Jon Jensen
Counsel

O P I N I O N

This appeal is made pursuant to section 25666 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Credit Bureau Central, Inc. against proposed assessments of additional franchise tax in the amounts of $812.17, $2,048.33 and $458.44 for the income years ended June 30, 1973, 1974, and 1975, respectively.

The issue for determination is whether appellant was engaged in a unitary business with its parent and the parent's other subsidiaries. Hereinafter, appellant, its parent, and the other subsidiaries shall be referred to as "the affiliated group."

Appellant is a collection agency with three offices in California. During the years in issue, it was a wholly-owned subsidiary of Daisy Corporation (hereinafter referred to as "Daisy"), whose offices were in Augusta, Georgia. Daisy was also the sole owner of thirteen other subsidiaries engaged in the collection field. Additionally, Daisy owned and operated three wholesale bakeries in Tennessee and South Carolina during 1973 and 1974.

All of Daisy's wholly-owned subsidiaries, including appellant, were engaged in what appellant describes as "collection agency type functions." Except for its bakery operation, the only activity which Daisy conducted was the management of its subsidiaries engaged in the collection agency business. Daisy's corporate management set overall management policy for each of its subsidiaries, as outlined by its board of directors, and provided sales level, budget, and profit goals for each member of the affiliated group. Additionally, Daisy closely supervised the implementation of its policies by the subsidiaries.

Appellant and its affiliates all shared common directors and officers with Daisy. Specifically, Dick Brown served as Daisy's president, Robert Harkrider was vice-president and treasurer, and Peggy Covert was secretary. The same three individuals held similar offices in each of the fourteen operating subsidiaries and constituted three of the four members of the boards of directors of each corporation forming part of the affiliated group.

Intercompany accounts existed between Daisy and each of its subsidiaries engaged in the collection agency business. These accounts permitted Daisy to withdraw profits from its subsidiaries as well as to charge them for management services. With the exception of its bakery operation, Daisy's income was derived from these management fees, which were determined by apportioning Daisy's expenses among the subsidiaries. in the same proportion as the total management services with which each subsidiary had been provided.

Daisy, as previously' noted, engaged in no collection activities of its own; those activities were conducted by its operating subsidiaries. Daisy did, however, provide services of noteworthy importance to its wholly-owned subsidiaries. It was largely responsible for the preparation of their monthly financial statements and maintained an internal audit department for their review. Daisy was also apparently responsible for preparing reports for its shareholders, in which it indicated the business prospects for the affiliated group, for handling securities transactions affecting the affiliated group, and for insuring compliance with regulatory requirements. Additionally, appellant has indicated that Daisy purchased insurance for its subsidiaries and that it was directly responsible for the recruitment and dismissal of high-level subsidiary personnel. In other areas, the operations of the affiliated group were not characterized by any degree of centralization. The individual subsidiaries did not exchange personnel or the debtor accounts which they serviced; the affiliated group did not conduct centralized advertising or solicit business as a whole; and there is no evidence that Daisy put its financial resources at the disposition of its subsidiaries.

Daisy, a publicly held corporation subject to the rules and regulations of the Securities and Exchange Commission, employed the accounting, firms of Ernst and Ernst in 1973 and Phillips and Curtis in 1974 and 1975 to perform year-end audits and certify its annual financial statements. Presumably, the same accounting firms prepared consolidated statements to be presented to Daisy's stockholders in its annual reports.

For the years in issue, appellant computed its California income by use of the separate accounting method. Respondent determined that appellant, Daisy, and the other subsidiaries engaging in the collection agency business were involved in a single unitary business. It further determined that Daisy's bakery operation was not part of the unitary business. However, despite ample time to do so, appellant failed to produce any records segregating Daisy's bakery operation from that of the affiliated group. Consequently, respondent was unable to exclude it from the unitary operation of the affiliated group for purposes of calculating the proposed assessment here in issue.

When a taxpayer derives income from sources both within and without California, it is required to

measure its California franchise tax liability by its net income derived from or attributable to sources within this state., (Rev. & Tax. Code, § 25101.) If the taxpayer is engaged in a unitary business with an affiliated corporation or corporations, the amount of business income attributable to California sources must be determined by applying an apportionment formula to the total income derived from the combined unitary operations of the affiliated companies. (See Edison California Stores, Inc. v. McColgan, 30 Cal.2d 472 [183 P.2d 16] (1947); John Deere Plow Co. v. Franchise Tax Board, 38 Cal.2d 214 [238 P.2d 5691 (1951), app. dism., 343 U.S. 939 [96 L.Ed. 1345] (1952).)

The California Supreme Court has determined that a unitary business is conclusively established by the existence of: (1) unity of ownership; (2) unity of operation as evidenced by central purchasing, advertising, accounting, and management divisions; and (3) unity of use in a centralized executive force and general system of operation. (Butler Bros. v. McColgan, 17 Cal. 2d 664 [111 P.2d 334] (1941), affd., 315 U.S. 501 [86 L.Ed. 991] (1942).) The Supreme Court has also held that a business is unitary when the operation of the business within California contributes to, or is dependent upon, the operation of the business outside the state. (Edison California Stores, Inc. v. McColgan, supra, 30 Cal.2d 472, 481.) These principles have been reaffirmed in later cases, (Superior Oil Co. v. Franchise Tax Board, 60 Cal.2d 406 [34 Cal.Rptr. 545, 386 P.2d 331 (1963); Honolulu Oil Corp. v. Franchise Tax Board, 60 Cal.2d 417 [34 Cal.Rptr. 552, 386 P.2d 40] (1963).)

The existence of a unitary business may be established if either the three unities or the contribution or dependency test is satisfied. (Appeal of F. W. Woolworth Co., Cal. St. Bd. of Equal., July 31, 1972; Appeal of Browning Manufacturing Co., et al., Cal. St. Bd. of Equal., Sept. 14, 1972; Appeals of the Anaconda Company, et al., Cal. St. Bd. of Equal., May 11, 1972.) Respondent concluded that appellant and the remainder of the affiliated group were engaged in a single unitary business under both of the above described tests. In reaching that conclusion, respondent relied principally on the following factors: total ownership of appellant and its affiliated subsidiaries by their mutual parent, Daisy; an integrated executive force which controlled the major policy decisions of the affiliated group: the operation of similar businesses by

appellant and Daisy's other operating subsidiaries and the sharing of know-how between the subsidiaries; common professional advisers: and centralized services provided by the parent on behalf of its subsidiaries.

It is appellant's position that, in order for respondent to prevail, it must be established that it had direct unitary relationships with each of Daisy's other subsidiaries. Appellant maintains that such a showing has not been made and that it operated independently from its affiliated subsidiaries. We have resolved this issue adversely to the taxpayer in prior appeals. (Appeal of Arkla Industries, Inc., Cal. St. Bd. of Equal., Aug. 16, 1977; Appeal of Beecham, Inc., Cal. St. Bd. of Equal., March 2, 1977; Appeal of Grolier Society, Inc., Cal. St. Bd. of Equal., Aug. 19, 1975; Appeal of Monsanto Co., Cal. St. Bd. of Equal., Nov. 6, 1970.) It is unnecessary to find a direct unitary relationship between appellant and its affiliated subsidiaries; it is sufficient that the unitary relationship be indirect. (Edison California Stores, Inc. v. McColgan, supra; Appeal of Arkla Industries, Inc., supra.) In Edison California Stores, supra, the California Supreme Court held that where a parent corporation performed centralized management, purchasing, advertising, and administrative services for its fifteen selling subsidiaries located throughout the United States, a unitary business existed. It was readily apparent in that case that there was no direct unitary relationship between the California selling subsidiary and the other selling subsidiaries located throughout the country. Nevertheless, the court found that they were all part of the same unitary business. Accordingly, respondent must prevail if it is established that appellant's operations were unitary with the activities of its parent, Daisy, and thereby indirectly unitary with its affiliated subsidiaries.

Appellant also argues, in reliance on our decisions in Appeal of Lear Siegler, Inc., decided April 24, 1967, Appeal of Simco, Inc., decided Oct. 27, 1964, and Appeal of Highland Corp., decided May 20, 1959, that the mere fact that Daisy's corporate management set overall management policy for each of its subsidiaries is an insufficient basis upon which to rest a finding that its operations were unitary with the remainder of the affiliated group. While we agree with appellant that the above mentioned cases may be cited for that proposition, that is not the factual situation with which we have been presented. Rather, as we shall

discuss below, the facts of this appeal lead to the conclusion that appellant was engaged in a unitary business with its parent and affiliated subsidiaries under either the three unities test or the contribution or dependency test.

The presence of unity of ownership, a prerequisite to the existence of a unitary business under either the three unities or the contribution or dependency test, is not contested.

Appellant has readily acknowledged that Daisy's board of directors set overall management policy for each of its subsidiaries, including appellant, and that it closely supervised the implementation of its policies by the subsidiaries. Furthermore, it admits that there was present among the affiliated group an almost completely integrated executive force which was responsible for centralized management of the entire group of affiliated corporations.

The courts and this board have repeatedly held that the integration of executive forces is an element of exceeding importance and constitutes compelling evidence of a unitary business operation. (See, e.g., Chase Brass & Copper Co. v. Franchise Tax Board, 10 Cal.App.3d 496 [87 Cal.Rptr. 2391, app. dism. and cert. den., 400 U.S. 961 [27 L.Ed. 2d 381] (1970); Appeal of Grolier Society, Inc., supra; Appeal of Monsanto Company, supra.) The degree of integration of the executive forces present in the instant appeal is greater than that evident in any of the above cited cases. The presence of interlocking officers and directors who made major policy decisions for the entire affiliated group is sufficient to show unity of use. (Appeal of The O.K. Earl Corporation, Cal. St. Bd. of Equal., April 6, 1972.) Likewise, the centralized services provided by Daisy on behalf of its subsidiaries are another factor indicating unity. (Butler Bros. v. McColgan, supra; Appeal of Harbison-Walker Refractories Company (on rehearing), Cal. St. Bd. of Equal., Feb. 15, 1972.) The providing of such centralized services is sufficient to satisfy the operational unity requirement of the three unities test. (Appeal of The O.K. Earl Corporation, supra.) Such indications of a unitary business operation are especially compelling when, as in this appeal, the taxpayer acknowledges the importance of the central direction provided by the integrated executive force and concedes that the parent did provide centralized services of significant importance to its subsidiaries.

Appellant has stated that all of Daisy's subsidiaries were engaged in the collection agency business. It asserts, however, that they were involved in different areas of the collection field and that there was no interdependence or interrelationship between their separate operations. An examination of appellant's claim reveals that the distinctions it has attempted to draw between the subsidiaries' business operations are of minimal significance. Appellant has failed to demonstrate that there is any substantive difference between the operation of a collection agency involved in general collection services and one which performs such services for a public utility or another which uses computerized letter writing and notice mailing to facilitate its operations.

We have previously held that where members of an affiliated group share common officers and directors while engaging in generally the same type of business, a reasonable inference can be drawn that the affiliated group benefited from the exchange of significant information. (Appeal of Maryland Cup Corporation, Cal. St. Bd. of Equal., March 23, 1970; Appeal of Anchor Hocking Glass Corporation, Cal. St. Bd. of Equal., Aug. 7, 1967.) In view of the similarities evident in the conduct of the subsidiaries' businesses and the high degree of integration present in the executive forces of the affiliated group, it is impossible to avoid the inference that there was a mutually beneficial exchange of information and know-how among these executives.

In numerous prior cases the unitary features evident in the operation of the affiliated group, when viewed in the aggregate, have been found sufficient to satisfy the three unities test and, furthermore, to demonstrate a degree of mutual dependency or contribution sufficient to compel the conclusion that a unitary business existed. (See, e.g., Chase Brass & Copper Co. v. Franchise Tax Board, supra; Appeal of Maryland Cup Corporation, supra; Appeal of Harbison-Walker Refractories Company (on rehearing), supra; Appeal of The O.K. Earl Corporation, supra.) Respondent's determination that appellant is engaged in a unitary business with its parent and affiliates is presumptively correct, and the burden of showing that such determination is erroneous is upon appellant. (Appeal of John Deere Plow Co. of Moline, Cal. St. Bd. of Equal., Dec. 13, 1961.) Although appellant contends that, as a matter of fact, the operations of the affiliated group did not constitute a single unitary business, it has not provided the

factual evidence needed to support its position. Thus, we must conclude that appellant has failed to carry its burden of proof.

Appellant has complained that the amounts of the proposed assessments are obviously in error because they were calculated by including Daisy's bakery operation in that of the affiliated group. Respondent, as noted earlier, determined that the bakery operation was not a part of the unitary operation, but included it in the unitary business because appellant failed to provide any information enabling respondent to segregate the bakery operation from the affiliated group. Respondent's determination cannot be successfully rebutted when the taxpayer fails to present relevant evidence as to the issue in dispute. (Cf. Banks v. Commissioner, 322 F.2d 530 (8th Cir. 1963); Estate of Albert Rand, 28 T.C. 1002 (1957).) When, as in this appeal, the taxpayer has the needed information or has access to the necessary evidence but does not produce it, he is not in a position to complain of adverse consequences. (Stanley Rosenstein, 32 T.C. 230 (1959); Appeal of Henrietta Swimmer, Cal. St. Bd. of Equal., Dec. 10, 1963.)

For the reasons expressed above, respondent's action in this matter will be sustained.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Credit Bureau Central, Inc. against proposed assessments of additional franchise tax in the amounts of $812.17, $2,048.33 and $458.44 for the income years ended June 30, 1973, June 30, 1974, and June 30, 1975, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 2nd day of February , 1981, by the State Board of Equalization, with Members Bennett, Nevins, Reilly and Dron,enburg present.

Ernest J. Dronenburg, Jr. , Chairman

William M. Bennett , Member

Richard Nevins , Member

Goerge R. Reilly , Member

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